THE GROWING IMPORTANCE OF 'MANAGED MONEY'

By Andrew Singer


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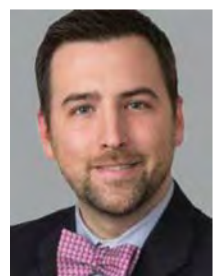
Timothy P. Munsie


Terrance Hughes

There may be no more potent sign that bank brokerage programs have arrived than the growing importance of "managed money."

Managed money,[1] also called advisory or fee-based business, was once the province of wirehouses, registered invesmtnet advisors (RIAs) and private banks. But it has been embraced in recent years by many retail bank investment programs and numbers of credit unions, too.

BISRA's monthly and quarterly benchmark data show a consistent growth of the managed money component in bank brokerage programs, even as transactional products like fixed and variable annuities tread water.

In the first quarter of 2010, for example, managed money (exclusive of trailer fees) accounted for only 5 percent of program revenues at bank brokerage programs, according to BISRA. By the third quarter of 2015, however—five and a half years later—managed money

1. Investopedia defines managed money as "a means of investment where the investor, rather than buying and selling their own securities, places their investment funds in the hands of a qualified investment professional for a predetermined annual fee."

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accounted for 23 percent of program revenues. Also note that during the same five-and-a-half-year period, fixed annuities fell from a 25 percent to 20 percent revenue share, and variable annuities ebbed from a 19 percent share to 16 percent.

Infinex Financial Group (Meriden, Connecticut), a third-party marketing firm, has gone through the request for proposal (RFP) process a number of times this past year with banks—particularly after its acquisition of Essex National Securities, announced in May 2015—and each time, managed money has been a top three priority among the soliciting bank, recounts Timothy P. Munsie, vice president, director of Advisory Services at Infinex—some indication of how big managed money has become for bank investment programs.

“It’s a growth business for us, even if it’s not necessarily a new business,” said Douglas Singer, president of The Huntington Investment Company, a subsidiary of Huntington Bancshares. Recently, the Ohio-based bank “restoked the fires,” adding new products and services to its advisory platform. “We’re adding capabilities to the platform, we’ve developed a more robust platform,” Singer, a senior vice president with Huntington Investment Company, the wholly-owned broker/dealer (B/D) subsidiary of Huntington Bancshares Inc. (Columbus, Ohio), told *BISA Magazine*.

There’s been a shift in the customer mindset in recent years, Singer noted. “When I first started, almost all business was transactional,” he said. Clients today, by contrast, often ask for a fee-based solution. They demand more clarity about fees, for instance, than was the case in the past.

Even credit unions are partaking. It’s long been assumed that credit unions, traditionally associated with working-class families, aren’t interested in managed money or advisory business, said Kevin Mummau, EVP, program development, CUSO Financial Services, LP (CFS)/Sorrento Pacific Financial, LLC (SPF). But they are. In fact, many of the third-party-marketing firm’s credit union clients exceed the firm’s commercial bank clients in advisory prowess. CFS’ commercial banks often sell packaged products like fixed and variable annuities overwhelmingly, he said.

A ‘Big Initiative’ at Wintrust

Wintrust Wealth Management offers a good illustration of how managed money has moved front and center among bank-owned B/Ds.

“Managed money is a big initiative for Wintrust Wealth Management,” said Terrance Hughes, director of sales, Wayne Hummer Investments, a Wintrust Wealth Management Company (Chicago). Wintrust Wealth Management is owned by Wintrust Financial Corp. (assets: $20 billion), which operates 15 banking subsidiaries in 140 locations in Illinois, Indiana and Wisconsin. Wintrust has 78 financial advisors. Almost all (about 95 percent) have advisory licenses, and the firm is “pushing hard” to make sure the remaining 5 percent secure those licenses soon.

What percentage of those with advisory licenses actually sell advisory products? “All do it,” Hughes answered.

Wintrust’s share of program revenue from advisory business is currently about 27 percent of total brokerage revenues, but share has been growing fast—about 3 to 5 percent a year. That is, advisory share went from 23 percent of program revenues at the beginning of 2015 to a 27 percent share at the end of the year. How high can it go, and what percentage is actually desirable? “I would love it to be 75 percent,” Hughes said.

Wintrust likes managed money because it offers more consistency in terms of revenue streams. Just look at August and November 2015. Those were incredibly slow months in terms of brokerage business, mainly because of the low interest rate environment. Investors were hard pressed to find yield. According to Hughes, his firm's investment sales dropped in both August and November. Monthly vagaries are much less of an issue, however, if clients are in a fee-based structure—where they pay annual fees based on assets under management (AUM) instead of paying commissions on individual trades, the more traditional approach in bank investment programs.

Yes, banks like managed money because it provides a more quantified, more consistent revenue stream, Hughes continued, but it also reduces potential conflicts of interest on the part of advisors. They are not tempted to favor high-commission products over low-commission products. Nor do advisors hesitate if a client's portfolio needs to be rebalanced. Transaction fees are a non-issue because they are included in the annual management fee.

This last factor is important because "80 percent of the success of a portfolio is based on allocation," Hughes said. Markets change and portfolios can quickly get out of kilter. Hughes doesn't want his advisors to think twice about rebalancing—they should just do it when it's appropriate.

According to Munsie, banks like managed money because it increases their customer base, helps to retain existing clients (i.e., stem client attrition) and increases revenue.

And it's not just commercial banks that have embraced advisory. As noted, credit unions, too, are now in the managed money business. Things began around 2008, Mummau said. What credit unions like about advisory is that it promises a different kind of relationship with clients. They are sitting alongside the advisor, not on the opposite side of the table, he said.

Which Advisors are Most Successful?

What type of advisor thrives with fee-based products? "Advisors who take a (financial) planning approach are most effective," Munsie said. Can a traditional transaction-type advisor make the transition to fee based? Absolutely, he answered, even so-called "dinosaurs" that have been selling transaction products for decades. He's seen many success stories in recent years. A traditional broker can always find "pockets of (fee-based) business within an existing book," he asserted, though it won't happen immediately. It requires a sustained effort over time.

What is a good mix of transaction and fee-based business for a bank investment program? If a program can get to 50 percent from managed money, that's great, according to Munsie. The No. 1 hurdle to overcome "is the advisor's need for immediate income," he added. The bank can help by adding some incentives. What's critical, however, is to make the advisor believe it's a long-term plan.

A Three-Legged Stool

The key to success is a three-legged stool, said Hughes, consisting of training, adherence and incentives. You need the right incentives so you don't inadvertently raise compliance issues. But what you're really looking for is a behavioral change. This isn't a one-off process. "You need to talk and talk every day," Hughes said.

Huntington Bank has a robust training and certification process, said Singer, which includes in-person training with a certification test that's been created by the institution. Almost all of Huntington's 180 financial advisors have Series 65/66 securities licenses and can sell fee-based products, although not all sell at present. Still, Singer has seen an increase in advisors considering fee-based solutions in the past year.

Singer was not prepared to say that advisory solutions are better than transactional product solutions, though. "In most cases, clients want and need both," he said. As for one oft-cited reason in favor of fee-based business—that it puts the advisor and client on the same side of the table (e.g., eliminating churning): "I don't buy that," Singer said. "We have an obligation to sit on the same side of the table *whatever* we sell."

Nor, in Singer's view, is there some ideal mix of transactional and fee-based business. "There's not a fear that we get too high (i.e., too high a percentage of fee-based products and services) or too low," he said.

In 2010, managed money accounted for only 5 percent of program revenues at bank brokerage programs. Five and a half years later, managed money accounts for 23 percent of program revenues, according to BISRA.

Wintrust likes managed money because it offers more consistency in terms of revenue streams, said Terrance Hughes, director of sales, Wayne Hummer Investments.

Recruiting Wirehouse Brokers

As noted, Wintrust draws about 27 percent of retail brokerage revenues from fee-based products, which is not unusually high, even among banks. But that number is somewhat skewed, Hughes added, because Wintrust's *nonbank*-based brokers, part of a legacy business, do an unusually low percentage of fee-based. More recently hired advisors for the bank-based program segment do a lot more fee-based business, by comparison. Wintrust is trying to get its nonbank-based advisors to do more fee-based business, Hughes said, but it is difficult because many have robust books of business that they don't want to tamper with.

Wintrust doesn't typically recruit advisors from other bank programs. They prefer financial advisors (FAs) with wirehouse backgrounds, who are already conversant with advisory products, Hughes said.

Even though Wintrust doesn't offer big on-loading packages, "we've been able to get them," said Hughes of the wirehouse reps. Wintrust can offer an entrepreneurial, open-architecture product environment with lots of support, like a good help desk, sales assistants and the like. They offer an "FA-centric" shop, according to Hughes. Moreover, "our brand resonates well in the Chicago area, and we can usually get an audience" when recruiting experienced reps. The advisory share of total revenues has increased as Wintrust has been recruiting aggressively recently in places like Indiana and Wisconsin, along with Illinois.

Does a Client Really Belong?

Wintrust is careful to ensure that a client really belongs on a managed money platform. It isn't right for every client. "We are acutely aware of our responsibilities as a fiduciary," Hughes said.

How to do this? Some banks look closely at the number of transactions a year conducted on behalf of a client. Too few and the client may be overpaying for advisory. Others provide a script in which a client has to acknowledge receiving advice. It varies bank by bank.

Wintrust monitors accounts quarterly, looking at things like the number of trades conducted. Advisors, too, are required to review investment returns based on the goals and risk tolerance that have been established based on prior conversations with the client. Every year, the bank presents its advisory clients with a side-by-side comparison: This is what the client would have paid in fees and charges as a transactional customer; this is what the client paid as an advisory client.

If it's determined that a broker really isn't providing sufficient advice for a client to be in advisory, the FA has six months to fix matters. If they don't, "then we will do it," Hughes said. The broker, in other words, has at most 18 months to get it right.

If the FA is only doing four trades a year on behalf of a client, for example, each of which might cost $75, the advice being offered is arguably not "robust enough" to justify an annual management fee on assets of 1 percent (or thereabouts), Hughes suggested.

The Importance of Peers

Recurring revenue is now at 33 to 34 percent of total revenues at CUSO Financial Services' client credit unions, according to Mummau, although most of that is still in the form of trailers (as opposed to managed money fees). Still, the advisory component alone is 12.5 percent to 13 percent of overall program revenue, and it is growing vis-à-vis the trailer component, he noted.

A key reason managed money is taking hold in credit unions: Some credit union-based reps have had success, and their fellow reps have taken notice. "Reps always need a peer to do it first," Mummau said. When a rep is successful with advisory, other reps notice that success. They see that adding a mutual fund or exchange-traded fund (ETF) wrap account to their product "quiver" might be a good idea.

The wrap accounts are, in fact, the biggest advisory product in the credit unions, Mummau said. They don't have many discretionary-type accounts where the financial advisor acts as portfolio manager.

Overall, "The biggest hurdle is getting them to stick their toe in the water," Mummau said.

Still, "Once they do a couple of accounts, the reps say, 'Wow, next quarter I'll begin with this…,'" Mummau said.

What many reps don't realize, Mummau added, is that some prospects are walking out the door *because you [the bank] don't offer advisory*. He recounts how a new advisor replaced an experienced (and quite successful) transaction-type advisor who retired.

She had all the old advisor's notes. She talked about advisory to one client who had met with the retiring advisor only 12 months earlier. The client soon brought over $1 million that she had invested through a wirehouse. She wanted to keep it at her credit union. The reason the client never did this before was because the old advisor never mentioned managed money solutions. The client had no idea that the credit union offered these products and services.

Overall, more than half of CFS' client credit unions are doing some advisory business, Mummau estimated, and if one looks at new invested dollars coming in in 2016, advisory has surpassed variable annuities, he said, although variable annuities (VAs) are still ahead in revenues.

"The best kept secret is being a rep in a credit union," Mummau added. One of CFS' top reps does $1.5 million in annual revenue, he noted, of which $1.3 million is recurring. Credit unions offer a great opportunity for representatives— in no small part because so many clients have a strong relationship with their credit unions, a deeper relationship than that of bank clients with *their* institution, arguably. Advisory fits in with this.

How Can a Rep Get to $750,000 a Year?

Persuading transaction-type reps to sign on to advisory is a continuous challenge, however. Munsie offered this argument: A good bank broker these days is one who does $450,000 or more annually in GDC, arguably. Many do this by selling transaction products like fixed and variable annuities, real estate investment trusts (REITs), unit investment trusts (UITs), and so on. But how does a bank-based broker get to $750,000 a year? The advisor probably can't sell more transaction products, which have to be replaced each year given their one-off nature. "They have to change something," Munsie said. His firm recommends that advisors approach clients with a financial plan, one that can bring in some of those assets held outside of the bank. The FA should set three-, five- and seven-year goals. Eventually, "You'll get another $450,000 coming through recurring revenue," Munsie said. This is how they do it now at many independent brokerage firms, as well as at some big banks like Citibank and Wells Fargo, he suggested.

"There may be a run-off [in rep compensation] in year one, but then it increases exponentially," Munsie said. Moreover, clients with managed money accounts tend to stay with the bank longer, reducing client attrition, he added.

Wrap Accounts Most Common

What about product? What are the leading managed money solutions in bank programs? Most successful banks have a third-party-managed mutual fund wrap solution, Munsie said. Separately managed accounts (SMAs) may be offered, but Munsie sees SMAs used mostly for complex tax planning for customers with $1 million or more in investable assets. The overlay fee with a SMA, after

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all, can be 50 basis points, while a third-party-managed mutual fund (MF) wrap may charge only 20 basis points for the overlay. Indeed, noted Munsie, an actively managed ETF or MF wrap account can be less expensive fee-wise than a static, traditional C-share mutual fund product.

At Wintrust, a popular advisory "solution" is a wrap mutual fund that is overseen by Russell Investments (Pathways) with a $25,000 minimum account size. Also popular is a kind of SMA (Fundsource) that requires an investment of between $25,000 and $250,000. Only 5 percent of brokers are using a discretionary program called Private Investment Manager (PIM), in which FAs act as portfolio managers, but that is the fastest growing solution, especially among recently hired advisors.

At Huntington Bank, a mutual fund wrap account is popular with clients without much experience with managed money solutions, said Singer. More sophisticated clients might gravitate to unified managed accounts (UMAs) or SMAs. "It's not a one-size-fits-all" situation, he said.

Keys to Success

How does a bank build a successful fee-based brokerage business? "It starts and ends with education and training," Singer said. You can't just train an advisor once and be done with it. "It's an ongoing process." Advisors need to stay current with product offerings and how products may or may not be impacted by the economy, for example. It requires continual coaching by regional managers.

As noted, brokers worry that suddenly migrating to a fee-based business will result in a hit to their revenues, but Munsie keeps telling them there is no need to cannibalize your income. Brokers just need to approach their existing customers differently. Brokers begin by asking: How does this piece fit into your overall goals, whether it be retirement, saving for college or something else. If brokers do this, they will identify other outside assets, Munsie asserted.

Mummau told his advisors they don't need to change 100 percent all at once. Look at it as adding another arrow to your quiver. He recommends they try it with 10 percent of their books. In the first year, the overall compensation may drop a little bit, but then the advisory pile will begin to grow.

Reps talk among themselves, Hughes noted, echoing an earlier point by Mummau If a rep has success, he or she talks about it, and peers soon catch on. Some of Hughes' bank reps work on the same floor within a building. They hear about the success reps are having with advisory products, and they want to copy it. Success breeds more success. ▲

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